Before the
Federal Communications Commission
Washington, D.C. 20554

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

In the Matter of Application by Verizon for Authorization Under Section 271 of the Communications Act to Provide In-Region, InterLATA Services in the State of Rhode Island and Providence Plantations	)	CC Docket No. 01-324

REPLY COMMENTS OF WORLDCOM, INC. ON THE APPLICATION BY VERIZON FOR AUTHORIZATION TO PROVIDE IN-REGION, INTERLATA SERVICES IN RHODE ISLAND

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January 10, 2002

INTRODUCTION AND EXECUTIVE SUMMARY

Verizon has made no progress toward lowering its dramatically high unbundled network element ("UNE") rates in Rhode Island since initial comments were filed in this case. The Department of Justice has encouraged the Commission to focus on these rates; the critical switching rate in Rhode Island even exceeds the very high existing rates in New York and Massachusetts. The most notable event since initial comments, however, is the decision of the U.S. Circuit Court of Appeals for the District of Columbia Circuit which remanded the Commission's order in the Kansas-Oklahoma section 271 case for further consideration of the impact of a price squeeze on competitive local exchange carriers ("CLECs"). The question is whether, within the range of total element long range incremental cost ("TELRIC,") it is adequate to set rates at the high end if that causes a price squeeze which prevents widespread local competition.

This application currently presents an easy TELRIC case, in which Verizon is trying to get away with switching rates that exceed any that have ever been the basis of section 271 approval by the Commission, even in New York or Massachusetts. But even if Verizon were to reduce its Rhode Island switching rates to the level of New York or Massachusetts, its application should still be denied, for the dramatic price squeeze in which competitors are caught should require Verizon to be at the bottom of the reasonable range of TELRIC, rather than over the top.

Given the high UNE rates in Rhode Island – for both switching and loops – competitors would lose money on average on every line for every consumer every month. Indeed, the

TABLE OF CONTENTS

TABLE OF ATTACHMENTS

TAB	DECLARANT	SUBJECT
A	Reply Declaration of Vijetha Huffman	Pricing

Before the
Federal Communications Commission
Washington, D.C. 20554

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	)	
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This application currently presents an easy TELRIC case, in which Verizon is trying to get away with switching rates that exceed any that have ever been the basis of section 271 approval by the Commission, even in New York or Massachusetts. But even if Verizon were to reduce its Rhode Island switching rates to the level of New York or Massachusetts, its application should still be denied, for the dramatic price squeeze in which competitors are caught should require Verizon to be at the bottom of the reasonable range of TELRIC, rather than over the top.

Given the high UNE rates in Rhode Island – for both switching and loops – competitors would lose money on average on every line for every consumer every month. Indeed, the situation is so bad that the statewide gross margin is negative, meaning that on average a CLEC would lose money on every customer every month even before covering any of the $10 per month of costs necessary to account for customers who do not pay their bills, customer service and other so-called internal costs. This is true even though the retail rates in Rhode Island (that is, the total revenue per line) are greater than the comparable rates in Pennsylvania, Texas, Michigan, Illinois, and Florida, each of which WorldCom has entered.

Verizon's UNE rates need to be greatly improved. As explained in WorldCom's initial comments, this is not a theoretical exercise for WorldCom, for these excessive UNE rates prevent WorldCom from being able to bring local competition to the consumers of Rhode Island, just as they block WorldCom from entering the local residential market in Massachusetts. Pricing remains the single critical issue in Rhode Island for WorldCom, and until Verizon's above-cost prices are reduced to eliminate the price squeeze, its application for Rhode Island must be denied.

TABLE OF CONTENTS

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TAB	DECLARANT	SUBJECT
A	Reply Declaration of Vijetha Huffman	Pricing

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Washington, D.C. 20554

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VERIZON'S ABOVE-COST UNE RATES CREATE A PRICE SQUEEZE AND ARE NOT IN THE PUBLIC INTEREST

Pricing remains the central issue of concern in this application as Verizon has made no progress toward UNE rates that comply with the FCC's TELRIC requirements and the public interest requirements of the Telecommunications Act. All of the issues raised in WorldCom's initial comments still apply, and now the Department of Justice has encouraged the Commission to examine the concerns raised about Verizon's UNE rates. Verizon's UNE rates are too high to permit ubiquitous local residential competition anywhere in the state, depriving Rhode Island consumers of all the benefits of competition. The Commission should reject Verizon's section 271 application until it has corrected its UNE rates to reflect TELRIC in the range that will eliminate the price squeeze of competitors and permit broad scale local competition in Rhode Island.

As explained in the accompanying Reply Declaration of Vijetha Huffman, WorldCom would like to serve a broad range of customers in Rhode Island, and other states, by offering a package that includes local service to the mass residential market. Due to Verizon's high prices for UNEs, however, WorldCom is unable to do so. This is unfortunate for it deprives consumers of the opportunity to benefit from new and innovative products and to save money on their telephone bills. In addition, a strong local presence is essential to WorldCom's competitive success in providing service to residential customers, since many residential customers desire fully integrated telecommunications services, including local, long distance, and more. Huffman Reply Decl. ¶¶ 3-4.

There is a severe price squeeze in Rhode Island, which means that even a CLEC selling local residential service for the same price as Verizon would not make nearly enough money to pay for the cost of the elements it leases to provide the service and its own internal costs. Huffman Reply Decl. ¶ 9. Even in the most favorable zone, the gross margin between a CLEC's revenues and telco costs using UNE-P would be only $2.86 per line each month, which is not sufficient to cover a company's internal costs of more than $10 dollars per line each month.[1] Remarkably, in the other two zones the gross margin is <u>negative</u>, even before the CLEC covers any internal costs. In fact, the statewide gross margin is negative in Rhode Island, meaning that on average a CLEC would lose money on every customer every month even before beginning to cover <u>any</u> of its internal costs. This is true even though the retail rates in Rhode Island (that is, the total revenue per line) are greater than the comparable rates in Pennsylvania, Texas,

[1] The Huffman Reply Declaration explains the monthly revenue a carrier would receive if it provided basic local service with one feature at the same retail price Verizon charges, and then subtracts from that revenue the costs of the leased unbundled network elements. From that amount, <u>i.e.</u>, the gross margin, a carrier must then cover its own internal costs, which typically include marketing costs, customer service costs, costs associated with customers who

Michigan, Illinois, and Florida, each of which WorldCom has entered in whole or in part. Huffman Reply Decl. ¶ 9.

The price squeeze results from errors contained in the pricing methodology used to set both the switching and loop rates in Rhode Island, as discussed in WorldCom's opening comments in this proceeding. The switching rates are especially high, with switch ports averaging over $4.00 per month per line. Verizon's port charge in Rhode Island is double the Massachusetts rate and far higher than in any state that has been granted section 271 authority. The total switching rate (port plus usage) is extremely high and even exceeds the comparable rates in Massachusetts and New York, which are themselves excessive. Huffman Reply Decl. ¶ 10.

Verizon's loop rates in Rhode Island are also excessive due to improper assumptions about use of fiber feeder, failure to use GR-303 compliant digital loop carriers, improper assumptions for structure sharing, and reliance on low fill factors, as described in WorldCom's initial comments.

Unlike New York's high UNE rates that were specifically found by the New York commission and the FCC to permit local residential competition due to New York's generous retail rates, ubiquitous local residential competition is not possible in Rhode Island due to Verizon's UNE rates, as discussed above. As suggested by the D.C Circuit Court in Sprint Communications Co v. FCC, No. 01-1076, 2001 U.S. App. LEXIS 27292 (D.C. Cir. Dec. 28,

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don't pay their bills, and other operational costs. These internal costs exceed $10 per line per month, even apart from significant up front development costs. Huffman Reply Decl. ¶ 8.

2001), in the context of the price squeeze in Kansas-Oklahoma, rather than aiming for the high end of the reasonable TELRIC range (as viewed by the Commission), the Commission should require Verizon's rates to be at the low end of the range in order to eliminate the price squeeze and permit widespread local competition in Rhode Island. Verizon must establish prices that allow competitors to gain customers without losing money in order to achieve irreversible residential competition in Rhode Island. Huffman Reply Decl. ¶ 12.

Finally, while BOC applicants routinely claim that granting section 271 entry will have a dramatic effect on the local residential market, there is now enough experience to rely on facts rather than rhetoric. It turns out that the facts are relatively straightforward, and that section 271 entry does not have the magical impact that applicants claim. Applicants carefully choose to spotlight and extrapolate from a couple of states – specifically New York and Texas – where local competition was already well under way prior to section 271 authorization, and do their best to ignore the greater number of states where competition could not thrive before the section 271 application and cannot develop after section 271 entry, including Massachusetts, Kansas, Oklahoma, Missouri, Arkansas and Connecticut.

Quite simply, where barriers to entry such as anti-competitive pricing and discriminatory OSS are eliminated, WorldCom will use UNE-P – the only viable service delivery vehicle – to enter residential markets.[2] WorldCom offers local residential service using UNE-P in an

[2] Cable telephony is fine for the incumbent cable company that may choose to offer it, but typically adds – at most – a single additional local competitor to the marketplace, while UNE-P can be the basis for rapid and ubiquitous entry by multiple CLECs. It is well established that two competitors are not sufficient to bring adequate competition to a market, as illustrated in recent years by the cellular license duopoly that became markedly more competitive once additional carriers could enter.

increasing number of states in which conditions permit entry in at least some part of the state, namely New York, Texas, Pennsylvania, Michigan, Illinois, Georgia and even limited parts of Florida. WorldCom goes where it can reasonably hope to enter based on UNE rates and OSS, not where section 271 has been granted. WorldCom has entered many states that have not been granted section 271 authority (Michigan, Illinois, Georgia and Florida). Moreover, of WorldCom's entry states that have been granted authority (New York, Pennsylvania and Texas), WorldCom entered well before section 271 authority was granted, sometimes by more than a year. Section 271 approval has not caused WorldCom to enter any state: WorldCom has not entered Massachusetts, Kansas, Oklahoma, Missouri, Arkansas or Connecticut. WorldCom is unable to enter Rhode Island due to Verizon's above cost rates, which would not be altered by the grant of section 271 authority. Huffman Reply Decl. ¶ 6.

In short, if the section 271 carrot is removed, Verizon will have no incentive to eliminate the barrier to entry posed by high UNE rates.

CONCLUSION

Verizon's Rhode Island application should be denied.

Respectfully submitted,

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January 10, 2002

Certificate of Service

I, Vivian Lee, do hereby certify that copies of the foregoing Reply Comments of WorldCom, Inc. were sent via e-mail (as indicated) or first class mail to the following on this 10th day of January, 2002.

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Under Section 271 of the Communications	)	
Act to Provide In-Region, InterLATA	)	CC Docket No. 01-324
Services in the State of Rhode Island and	)	
Providence Plantations	)	
	)	

REPLY DECLARATION OF VIJETHA HUFFMAN
ON BEHALF OF WORLDCOM, INC.

Based on my personal knowledge and on information learned in the course of my duties, I, Vijetha Huffman, declare as follows:

1. My name is Vijetha Huffman. I am Senior Manager of Local Business Development for the Mass Markets Division of WorldCom. I am responsible for financial planning, operational and business analysis, and new market development in support of WorldCom's entry into the residential local business. This includes evaluating the financial viability of providing residential local service in markets that WorldCom has not yet entered and determining price changes necessary for WorldCom to enter. I have worked for WorldCom (and its predecessor MCI) for 6 years in a number of finance positions.

2. The purpose of my declaration is to explain why local service is critical to WorldCom's business plans for the residential market and how Rhode Island's network element pricing presents a price squeeze for competitors and prevents the development of local competition in the state.

I. LACK OF MARKET ENTRY IN RHODE ISLAND VIA UNE-P

3. WorldCom would like to serve a broad range of customers in Rhode Island and other New England states, offering a package of services to the mass market that includes local service. However, WorldCom is unable to enter the local residential market in Rhode Island because of Verizon's high prices for UNEs.

4. A strong local presence is essential to WorldCom's competitive success in providing service to residential customers. Many residential customers are seeking fully integrated telecommunications services, including local, long distance, and Internet access. Customers also seek the opportunity to benefit from new and innovative products and to save money on their telephone bills. Thus, the ability to profitably offer integrated products is critical to WorldCom's plans to respond to the needs of its existing long distance customer base and to attract new customers.

5. UNE-P, the combination of all unbundled elements necessary to provide local service, is the only service-entry vehicle that WorldCom uses to offer local residential service, and it is the only service-delivery option that WorldCom currently views as even potentially viable. The UNE-P mode of entry provides WorldCom with greater flexibility than resale to offer innovative products and permits much faster and more pervasive market entry than a pure facilities-based offering. Moreover, when UNE prices are truly set at cost-based rates, CLECs generally can compete profitably with the ILECs. Where barriers to entry such as anti-competitive pricing and discriminatory OSS are eliminated, WorldCom will use UNE-P to enter residential markets.

6. UNE-P is the means that WorldCom uses to provide local residential service in a growing number of states in which conditions permit entry in at least some part of the

state, and now includes New York, Texas, Pennsylvania, Michigan, Illinois, Georgia and very limited parts of Florida. It is notable that WorldCom has entered many states that have not been granted section 271 authority (Michigan, Illinois, Georgia and Florida), and of the entry states that have been granted authority (New York, Pennsylvania and Texas), WorldCom entered well before section 271 authority was granted, sometimes by more than a year. On the other hand, section 271 approval has not caused WorldCom to enter any state: WorldCom has not entered Massachusetts, Kansas, Oklahoma, Missouri, Arkansas or Connecticut. As noted above, WorldCom is unable to enter Rhode Island due to Verizon's above cost rates, a fact that would not change by the grant of section 271 authority.

II. PRICE SQUEEZE IN RHODE ISLAND

7. WorldCom generally will not sell goods or services unless it believes it can do so profitably. Selling basic residential service profitably in Rhode Island using Verizon's facilities currently is not feasible for competitive carriers, including WorldCom.

8. As seen in Attachment 1 hereto, there are three zones in Rhode Island. These zones are urban, suburban and rural. Attachment 1 demonstrates the monthly revenue a carrier would receive if it provided basic local service with one feature at the same retail price Verizon charges, and then subtracts from that revenue the "telco" costs, or, in other words, the costs of the leased unbundled network elements. From that amount, i.e., the gross margin, a carrier must then cover its own internal costs. Internal costs typically include marketing costs, customer service costs, costs associated with customers who don't pay their bills, and other operational costs, and exceed $10 per line per month, even apart from significant upfront development costs.

9. As shown on Attachment 1, even a CLEC selling local residential service for the same price as Verizon would not make nearly enough money to pay for the cost of the elements it leases to provide the service and its own internal costs. For example, in the most favorable zone, the gross margin between a CLEC's revenues and telco costs using UNE-P would be only $2.86 per line each month. Clearly, a margin that small is insufficient to cover a company's internal costs. The problem is even more dramatic in the other zones, where the gross margin is negative, even before the CLEC pays any of its internal costs. Indeed, the statewide average gross margin is negative, meaning that on average a CLEC would lose money on every customer every month even before beginning to cover any of its internal costs. This is true even though the retail rates in Rhode Island (that is, the average total revenue per line) are greater than the comparable rates in Pennsylvania, Texas, Michigan, Illinois, and Florida, each of which WorldCom has entered in whole or in part.

10. As discussed in WorldCom's opening comments in this proceeding, the pricing methodology used to set the rates in Rhode Island contains errors that led to high rates that do not support statewide competition. The switching rates are especially high, with switch ports averaging over $4.00 per month per line. As shown on Attachment 2, Verizon's port charge in Rhode Island is double the Massachusetts rate and far higher than in any state granted section 271 authority. The total switching rate (port plus usage) is extremely high and even exceeds the comparable rates in Massachusetts and New York, which are themselves far too high.

11. Verizon's loop rates in Rhode Island also exceed cost-based rates based on a proper TELRIC model, as discussed in WorldCom's initial comments. Verizon's loop

rates are inflated through improper assumptions about use of fiber feeder, failure to use GR-303 compliant digital loop carriers, improper assumptions for structure sharing, and reliance on low fill factors.

12. While New York's high UNE rates were specifically found by the state commission and the FCC to permit local residential competition given New York's generous retail rates, that is clearly not the case in Rhode Island, as shown above. Rather than aiming for (albeit missing) the high end of what the FCC considers the range of TELRIC, Verizon must be pointed to the low end of the range in order to eliminate the price squeeze and permit local competition in Rhode Island. To achieve irreversible residential competition in Rhode Island, Verizon must establish prices that allow competitors to gain a customer without losing money.

13. This concludes my declaration on behalf of WorldCom.

I declare under penalty of perjury that the foregoing is true and correct. Executed on January 10, 2002.

Vijetha Huffman

Rhode Island - Verizon (by zone)

	State	Urban	Suburban	Rural
Households (000) (1)	380			
Density	100%			
Local Revenue (2)	$24.44	$24.44	$24.44	$24.44
Access Revenue	$3.01	$3.01	$3.01	$3.01
Total Revenue	$27.45	$27.45	$27.45	$27.45
Switch Port	$4.15	$3.58	$4.47	$4.04
Loop	$13.93	$11.19	$15.44	$19.13
Switching & Transport (3)	$8.75	$8.75	$8.75	$8.75
DUF Charge (4)	$1.08	$1.08	$1.08	$1.08
Total Telco (5)	$27.91	$24.60	$29.73	$33.00
Gross Margin	($0.45)	$2.86	($2.28)	($5.54)

1 Households by telco zones not available.

2 Line fee reflects unlimited local plan, 1 feature (call waiting @ $3.65), and SLC.

3 Switching rates are equivalent to the VZN proposed rates in MA Telric Case.

4 DUF Rate is under reconsideration by the RI Commission.

5 Does not include NRC.

Note: Analysis does not include MCI or other CLEC internal costs (e.g., billing, customer service, sales/acquisition, bad debt)

CURRENT RHODE ISLAND RATES

	Switching	Port	Transport & other elements	Total: Switching/Port /Transport	Per MOU Switching Rate	Switch Features	DUF Charge
Rhode Island*	$7.16	$4.15	$1.59	$12.90	$0.002921		$1.08

** The "Per MOU Switching Rate" represents the originating switching rate. The terminating switching rate is $0.002563.*

MCI Entry States

State	Switching	Port	Transport & other elements	Total: Switching/Port /Transport	Per MOU Switching Rate	Switch Features	DUF Charge
Illinois (Flat rate)	$0.00	$5.01	$1.25	$6.26	$0.000000		$0.21
Illinois (SBC proposal)	$0.00	$3.16	$1.25	$4.41	$0.000000		$0.21
Michigan	$1.24	$2.53	$0.73	$4.50	$0.000522		$0.15
Texas *	$2.87	$2.90	$0.41	$6.18	$0.001042		$0.66
Georgia	$3.77	$1.79	$1.15	$6.71	$0.001633		$1.12
Pennsylvania **	$4.56	$1.90	$0.20	$6.66	$0.001802		$0.06
Florida	$1.81	$1.17	$0.99	$3.97	$0.000766	$2.26	$1.80
New York	$7.04	$2.50	$3.08	$12.62	$0.002986		$0.96
New York (ALJ Rec. Decision) ***	$2.63	$1.87	$1.44	$5.94	$0.001127		$0.22

** TX also has a separate call set-up charge of $.0010887/call*
*** The "Per MOU Switching Rate" represents the originating switching rate. The terminating switching rate is $0.001615.*
**** The "Per MOU Switching Rate" represents the originating switching rate. The terminating switching rate is $0.0010997; The port and switching rates represent a blended rate as these charges are de-averaged by Zone.*

OTHER 271 STATES

State	Switching	Port	Transport & other elements	Total: Switching/Port /Transport	Per MOU Switching Rate	Switch Features	DUF Charge
Massachusetts *	$7.94	$2.00	$2.24	$12.18	$0.003298		$0.96
Kansas *	$3.79	$1.61	$0.43	$5.83	$0.001613		$0.68
Oklahoma **	$4.86	$2.25	$0.60	$7.71	$0.002123		$0.66
Missouri **	$4.35	$1.91	$0.59	$6.85	$0.001878		$0.00
Arkansas *	$3.71	$1.61	$0.42	$5.74	$0.001604		$0.69

** The Switching Rate represents a blended rate as this charge is de-averaged by Zone.*
*** The Switching and Port Rates represent a blended rate as these charges are de-averaged by Zone.*

Notes:
- Switching, Port, and Transport figures represent per month, per line amounts.
- "Transport & other elements" includes blended and common transport, signalling, tandem switching, and EO and tandem shared trunk port.
- UNE telco rates represent RBOC portion of above states.